

1992

Bonneville International v. Utah State Tax Commission : Reply Brief

Utah Court of Appeals

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BONNEVILLE INTERNATIONAL
CORPORATION,

vs.

Respondent.

Priority 15

Petition for Review of the Final Order of the Utah State Tax Commission

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APR 8 1993

Mary Noonan
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Clerk of the Court

IN THE UTAH COURT OF APPEALS

BONNEVILLE INTERNATIONAL
CORPORATION,

Petitioner,

vs.

UTAH STATE TAX COMMISSION,

Respondent.

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No. 920775-CA

Priority 15

REPLY BRIEF OF PETITIONER

Petition for Review of the Final Order
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DETERMINATIVE STATUTES

Utah Code Annotated § 59-12-104 (1987 & Supp. 1991):

The following sales and uses are exempt from the
taxes imposed by this chapter:

* * * *

(15) Sales or leases of machinery and equipment purchased or leased by a manufacturer for use in new or expanding operations (excluding normal operating replacements, which includes replacement machinery and equipment even though they may increase plant production or capacity, as determined by the commission) in any manufacturing facility in Utah.

Manufacturing facility means an establishment described in SIC Codes 2000 to 3999 of the Standard Industrial Classification Manual 1972, of the federal Executive Office of the President, Office of Management and Budget. For purposes of this subsection, the commission shall by rule define "new or expanding operations" and "establishment." By October 1, 1991, and every five years thereafter, the commission shall review this exemption and make recommendations to the Revenue and Taxation Interim Committee concerning whether the exemption should be continued, modified, or repealed. In its report to the Revenue and Taxation Interim Committee, the tax commission review shall include at least:

- (a) the cost of the exemption;
- (b) the purpose and effectiveness of the exemption; and
- (c) the benefits of the exemption to the state.

ARGUMENT IN REPLY

The core issue in this case simply stated is whether Petitioner's Video West division (hereinafter "Bonneville"), which duplicates video tape, is engaged in manufacturing and thereby eligible for the tax exemption set forth in Utah Code Annotated § 59-12-104(15) (1987) for equipment purchases? That statute provides a tax exemption for equipment purchases to be used in a "manufacturing facility . . . described in SIC Codes 2000 to 3999 of the Standard Industrial Classification Manual 1972, of the federal Executive Office of the President, Office of Management and Budget." SIC Code 3652 applies to the manufacturing of "pre-recorded magnetic tape."

Bonneville believes it is entitled to the tax exemption set forth in Section 59-12-104(15), because video tape duplication is the manufacturing of pre-recorded magnetic tape. Respondent Utah State Tax Commission (the "Commission"), however, attempts to deny Bonneville the exemption contemplated in Section 59-12-104(15). The Commission claims that video tape duplication does not qualify as the manufacturing of pre-recorded magnetic tape, but rather should be defined, by inference to fall within the parameters of SIC Code 7819 which covers Hollywood-style motion pictures. The Commission's classification of Bonneville under the statute as a service industry rather than as a manufacturer disqualifies Bonneville for a tax exemption on its equipment purchases. The Commission's arguments, however, misinterpret the language and purpose of the statute and confuse its "real world" application.

I. The Commission Disingenuously Classifies Bonneville's Manufacturing Process As A Service

A. The Commission has accepted Bonneville's prima facie case that it is a manufacturer and therefore is eligible for the tax exemption.

The Commission has agreed that Bonneville was engaged in "manufacturing" video tapes [Record at 67]. Once the Commission established that Bonneville was engaged in manufacturing, the Commission's only discretion was to determine which category of manufacturing applied to Bonneville's activities. The Commission, however, criticized this straightforward analysis by stating:

What this suggestion fails to recognize is that "by its own terms, the 1972 SIC manual is intended to cover the entire field of economic activities." (R.9) Therefore, if a "manufacturing" activity is not included in the "manufacturing" classifications of the SIC Code, then, by the definitions of the SIC Code itself, the activity is not "manufacturing."

[Brief of Respondent at 12].

In making such an assertion, the Commission has applied backwards logic. The 1972 Manual does intend "to cover the entire field of economic activities." Given the ingenious nature of human creation, however, neither the 1972 Manual nor a soothsayer can set out expressly every known or about to be invented type of economic activity. Indeed, the very problem giving rise to this matter is that the SIC Code has never expressly included "video" tape duplication and

has only referred to manufacturing "pre-recorded magnetic tape" which is the same thing.¹

The SIC Code by its very nature requires such unidentified activities to be placed in a similar category by extrapolation. That such extrapolation is required in this instance does not somehow transmogrify manufacturing activities into services or production of original motion pictures as that contemplated in SIC Code 7819. In summary, the Commission has ignored the maxim that a rose by any other name is still a rose.

B. Bonneville's activities fall within the general guidelines for manufacturing activities identified in SIC Codes 2000 to 3999.

The Standard Industrial Classification Manual 1972 ("1972 Manual") sets forth manufacturing activities in its Division D. Those activities correspond to SIC Codes 2000 to 3999. Manufacturing is generally defined in the heading to Division D as:

Manufacturing production is usually carried on for the wholesale market, for interplant transfer, or to order for industrial users, rather than for direct sale to the domestic consumer. (emphasis added).

The heading to Division I of the 1972 Manual which covers the "service" industry in SIC Codes 7000 to 7999 conversely states:

This division includes establishments primarily engaged in providing a wide variety of services for individuals, business and government

¹ Although, as discussed below, Bonneville contends that its pre-recorded magnetic tape manufacturing is expressly included in SIC Code 3652. Therefore no extrapolation is required to bring Bonneville within the ambit of a manufacturing facility entitled to the tax exemption.

establishments, and other organizations. Hotels and other lodging places; establishments providing personal, business, repair, and amusement services; health, legal, engineering, and other professional services; educational institutions; membership organizations, and other miscellaneous services, are included.

Division I covers activities that can be classified not as manufacturing, but as services, sales, or other activities primarily directed at the retail or domestic market. Services are provided to the end user. Manufacturing is a wholesale, preliminary process directed to a re-seller who later markets to an end user. Bonneville's activities in manufacturing pre-recorded video tape are clearly carried out at the wholesale level and should be covered under Division D, SIC Code 3652 as a manufacturing activity.

C. Bonneville's activities fall outside the specific criteria for "Services Allied to Motion Picture Production" set forth in SIC Code 7819.

The Commission wrongly seeks to categorize Bonneville's video tape activities under SIC Code 7819, Division I. SIC Code 7819 encompasses activities related to the provision or servicing of motion pictures for sale to the public. In fact, the heading to the section under which SIC Code 7819 falls states:

Major Group 78 -- Motion Pictures

This major group includes establishments producing and distributing motion pictures, exhibiting motion pictures in commercially operated theaters, and furnishing services to the motion picture industry. The term "motion pictures" includes similar productions for television or other media using film, tape or other means.

This definition bears no believable resemblance to Bonneville's manufacturing of pre-recorded video tape for wholesalers. Bonneville is not producing, distributing, or exhibiting motion pictures. Nor is Bonneville providing services related to the creation of such films. It, consequently, would be improper to classify Bonneville's manufacturing activities under SIC Code 7819.

The Commission's argument that SIC Code 7819 more properly applies to the Bonneville process is not supportable. SIC Code 7819 only applies to services related to producing an original motion picture. The Bonneville process, to the contrary, involves manufacturing a pre-recorded product. The activities mentioned in Code 7819 involve service and support necessary to the production of an original motion picture product and have nothing to do with manufacturing. Where the Commission has become confused is equating "service" activities used to produce a single original product with activities that are used to manufacture multiple copies of the original. The process used to manufacture pre-recorded video tapes may possess some similarity with the process used for producing the original, but that does not make it a service rather than manufacturing. That is why SIC Code 3562 from the manufacturing section is the most applicable to Bonneville and not SIC Code 7819 which is from the service section.

II. Bonneville's Activities Are Covered By The Criteria For "Pre-recorded Magnetic Tape" Set Forth In SIC Code 3652.

To qualify under SIC Code 3652, a manufacturing facility must "engage principally in manufacturing pre-recorded magnetic tape." That is exactly what Bonneville does in as much as video tape is a magnetic tape.

The Commission's futilely attempts to distinguish Bonneville's video tape reproduction manufacturing facilities from its audio tape reproduction manufacturing facilities.² The Commission believes that video tape reproduction is not covered under the express wording of SIC Code 3652. Such a distinction is disingenuous. SIC Code 3652 makes no such distinction. As the Commission itself found, "The magnetic tape used by [Bonneville's audio reproduction facility] and [Bonneville] in their respective operations is essentially the same material." [Final Decision of Utah State Tax Commission dated September 3, 1992 at 2.]³

² The Commission also makes the odd argument that Bonneville's "processes are concerned with video tape duplication rather than tape manufacturing." Brief of Respondent at 8. The Commission's reading is entirely at odds with SIC Code 3652, as that Code makes no mention of "tape manufacturing" which is a different process -- covered under SIC Code 3679 -- than "manufacturing pre-recorded magnetic tape." Tape cannot be created from scratch in a pre-recorded form. In fact, mass tape duplication is the process by which pre-recorded magnetic tape is manufactured and therefore the exact process contemplated by SIC Code 3652.

³ As stated in Bonneville's main brief at pages 6 and 7, despite the virtually identical activities of Bonneville's two subsidiaries, the Commission allowed the exemption to only the one producing audio-only tapes.

Indeed, Bonneville's video manufacturing is covered under SIC Code 3652 as video tapes are in fact included within the broad definition of "audio" tapes. The addition of a video component to the tape does not alter this fact. In fact, so-called video tapes are really only video-enhanced audio tapes. Video tapes also can be, and have been, used for exclusively audio formats.

The Commission repeatedly speaks of the "important distinction between audio taping activities and video taping activities." They posit that the non-existent distinction somehow makes video tape reproduction non-exempt, e.g., Brief of Respondent at 10. The Commission, however, nowhere states what the important distinctions are, in fact the Commission provides no explanation of any real distinction. In the real world, both audio and video tapes are reproduced using the same fundamental technology and procedure. The Commission points out no important distinctions between the two types of tape because no such distinctions exist. Therefore, any distinction in the tax treatment of the two is wholly artificial, arbitrary, and without basis.

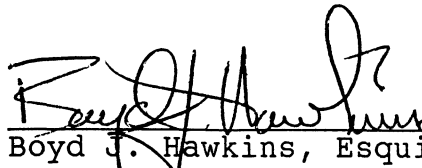
CONCLUSION

The Commission bases a large part of its argument on the case law that states that exemptions are to be construed strictly. That mandate does not, however, allow the Commission to engage in a stilted and unfair reading of the SIC Codes in an attempt to deny Bonneville a tax exemption that should plainly apply to its video tape

manufacturing. The Utah State Legislature broadly defined manufacturing activity in the statute. The Commission possesses no discretion to change the statute to one that is uncharacteristically harsh and unreasonable in its application. The Commission cannot now under guise of its mandate to construe exemptions strictly, remove all the play out of the SIC Code's definition of "manufacturing facility" which was meant to be broad and all encompassing. Bonneville's activities are clearly the manufacturing of pre-recorded magnetic tape contemplated by SIC Code 3652 and Utah Code Annotated § 59-12-104(15). Therefore, the Commission erred in its interpretation and application of the statute and its decision must be reversed.

DATED this 7th day of April, 1993.

BONNEVILLE INTERNATIONAL CORPORATION



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CERTIFICATE OF SERVICE

I hereby certify that two true and correct copies of the foregoing Brief of Petitioner were hand delivered this 8th day of April, 1993, to the following:

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A handwritten signature in cursive script, reading "Brent O. Hatch", written over a horizontal line.

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